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NO. 90-1621

Supreme Court, U.S.
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IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1990

VIRGINIA KNIGHT; EDMUND G. BROWN; WILSON RILES; RICHARD NEVINS; HOUSTON I. FLOURNOY; HAROLD J. POWERS,
Petitioners,

v.

BOARD OF ADMINISTRATION OF THE PUBLIC EMPLOYEES' RETIREMENT SYSTEM,
Respondent.

AMICUS CURIAE BRIEF OF ROBERT F. CARLSON AND CHARLES P. VALDES IN SUPPORT OF GRANTING PETITION FOR WRIT OF CERTIORARI IN ORDER TO PROTECT PENSION RIGHTS OF PUBLIC EMPLOYEES

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June 3, 1991

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	iii
INTEREST OF AMICUS CURIAE	1
SUMMARY OF ARGUMENT	4
ARGUMENT	9
I. THE LEGISLATIVE RETIREMENT SYSTEM IS A CONTRACT BETWEEN THE STATE AND ITS MEMBERS, PROTECTED FROM IMPAIRMENT BY THE CONTRACT CLAUSE OF THE UNITED STATES CONSTITUTION . . .	9
A. THE CONTRACT CLAUSE PROTECTS RETIREMENT BENEFITS.	9
B. A CONTRACTUAL PENSION OBLIGATION IMPLIES ADEQUATE FUNDING AND ADMINISTRATION OF THAT PENSION; AND FAILURE OR REFUSAL TO FUND THAT PENSION UNCONSTITUTIONALLY IMPAIRS THE RETIREMENT CONTRACT	12
C. THE LEGISLATURE INTENDED TO BIND ITSELF CONTRACTUALLY TO FUND THE LRS WHEN THE SYSTEM WAS ESTABLISHED	18
II. THE LRS IS NOT UNIQUE, AND ANY DEFINED BENEFIT SYSTEM MAY BE ADVERSELY AFFECTED BY THIS OPINION OF THE APPELLATE COURT.	20

TABLE OF CONTENTS (Continued)

Page

A. THE RESPONSES AND BRIEFS FILED BY REPONDENT BOARD IN THESE MATTERS HAVE BEEN A BREACH OF FIDUCIARY DUTY TO MEMBERS OF THE RETIREMENT SYSTEMS ITS REPRESENTS . . . 23

III. RETIREES' ACQUIRED CONTRACTUAL RIGHTS TO A SPECIFIC FORMULA FOR THE CALCULATION OF THEIR BASIC RETIREMENT BENEFITS BASED UPON THE FLUCTUATING FORMULA TIED TO INCUMBENT SALARIES WHICH CANNOT BE IMPAIRED 27

A. THE DIMUNITION OF A RETIREMENT ALLOWANCE BY AMENDING A RETIREES' FORMULA FOR THE CALCULATION OF RETIREMENT BENEFITS IS CONTRARY TO THE PUBLIC POLICY AND PURPOSE OF CALIFORNIA'S RETIREMENT LAWS. 29

CONCLUSION 32

TABLE OF AUTHORITIES

Page

Allen v. City of Long Beach
45 Cal.2d 128 (1955) 17

Betts v. Board of Administration
21 Cal.3d 939 (1978) . . . 6, 24, 27

Bellus v. City of Eureka
69 Cal.2d 336 (1968). 19

Bilyeu v. State Employees' Retirement System 58 Cal.2d 618 (1962) . . 30

California Teachers Ass'n v. Cory
155 Cal.App.3d 494 (1984) . . 13, 17

Carmen v. Alvord
31 Cal.3d 318 (1982) 10

Dombrowski v. Philadelphia (Penn. 1968)
245 A.2d 238 (Penn. 1968). . . 16

Gaglione v. Levitt
337 N.E.2d 592 (N.Y. 1975) . . . 14

Hittle v. Santa Barbara County Employees Retirement Association
39 Cal.3d 374 (1985) 24

Home Building & Loan Association v. Blaisdell 200 U.S. 398 (1934). . 11

Kern v. City of Long Beach
29 Cal.2d 848 (1947) . . . 10, 30, 31

Legislature of the State of California, et al. v. March Fong Eu, Secretary of State, et al,
SO19660 (1991) 6, 26

TABLE OF AUTHORITIES (Continued)

Page

CASES

Miller v. State of California 18 Cal.3d 808 (1977) 11

Olson v. Cory 27 Cal.3d 532 (1980). .6, 26

Sonoma County Organization of Public Employees v. County of Sonoma *23 Cal.3d 296 (1979)* 4

Strumsky v. San Diego County Employees Retirement Assn 11 Cal.3d 28 (1974) 10

Valdes v. Cory 139 Cal.App.3d 773 (1983). .1, 12, 17

Walsh v. Board of Adm. of PERS 3 Civil No. C008704 (1991) . . . 9

Weaver v. Evans 494 P.2d 693 (1972) . 15

OTHER AUTHORITIES

The United States Constitution

Article I, Section 10 . . 4, 6, 8, 9

Statutes

Government Code of California

Section 9558 19
Section 9359 20

State Controller, *State of California Eleventh Annual Report of Financial Transactions Public Retirement Systems Calendar Year 1988/Fiscal Year 88-89.* 22

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BRIEF OF ROBERT F. CARLSON AND CHARLES P. VALDES AS AMICUS CURIAE

INTEREST OF AMICUS CURIAE

The Amicus Curiae are members of Respondent Board of Administration of Public Employees' Retirement System (PERS). Robert F. Carlson is elected from the Retired Members of PERS. He has served on Respondent Board for 20 years, 10 years as president of the Board. He served 33 years with Caltrans as an attorney, his last years as Chief Counsel. In addition, he has been a professor of law at McGeorge School of Law for 15 years. Charles P. Valdes is, and has been, an attorney for Caltrans for the past 24 years. He was elected to the PERS Board from the Total Membership, and was the successful petitioner in the case of *Valdes v. Cory* (1983) 139 Cal.App.3d 773. He has served on the Respondent's Board for eight years and is the Vice-

President of the Board. The PERS Board administers the Legislators' Retirement System (LRS), the Judges' Retirement System (JRS), as well as the Public Employees' Retirement Systems including the statewide systems, and more than 1,160 other public retirement systems by contract.

Both men have followed the two cases now consolidated herein closely as well as other cases involving PERS. They were allowed to file an *Amicus Curiae* Brief in response to the questions posed by the Court of Appeal of the Third Appellate District in its letter of September 27, 1989 (Appendix G of the Petition for Writ, p 240g) and the reply contained in Respondent's Second Supplemental Briefs. As counsel for, and the, Amicus Curiae, they are familiar with the issues raised by the Lower Court's decision. In their

view if the decision of the Appellate Court herein is allowed to stand, the entire field of pension law in California will be destabilized. As elected members of the Respondent's Board, they believe it would be a breach of their fiduciary duty not to ask this Court to grant certiorari and reverse the Lower Court's opinion.

The opinion was originally certified for publication. It was printed in the advance sheets at 223 Cal.App.3d 527 and 273 Cal.Reporter 120. Although decertified for publication by the California Supreme Court, it will be reported in the bound volume of 273 Cal.Reporter 120 and the bound volume of the Pacific Reporter. This widely publicized decision gives a governingbody a radical and creative opportunity to seek to defeat retirement benefits of retirees at the expense of

all the members and retirees of public and private retirement systems with defined benefit plans in California and elsewhere. It will create chaos and a great deal of litigation!

SUMMARY OF ARGUMENT

I. The Supreme Court of California has held repeatedly that public employment does give rise to certain obligations which are protected by the Contract Clause of the Federal Constitution, (Art. I, Sec. 10), including the right to the payment of salary which has been earned and pension benefits. (*Sonoma County Organization of Public Employees v. County of Sonoma* (1979) 23 Cal.3d. 296, 308-309.) The Legislative Retirement System is a contract between the State and its members, protected from impairment by the Contract Clause. The Lower Court's decision departs radically from

the foregoing law established in California for more than fifty years. It has grafted on a new requirement for a pension benefit to be vested: that the retirement system have a continuing appropriation provision or be fully actuarially funded. This innovative proposition that if the Legislature has failed to enact a valid continuing appropriation provision for retirement benefits, or establish a particular funding mechanism to seek to achieve actuarial funding, then there is no enforceable contract obligation **by retirees** places all members and retirees of public retirement systems in jeopardy.

II. The decision demonstrates a deplorable ignorance of defined benefit retirement systems and their history generally, whether public or private. The LRS is not unique, and the decisional

law applicable to a retiree of LRS is also applicable to a retiree of any defined benefit plans, e.g., the universally cited case of *Betts v. Board of Administration* (1978) 21 Cal.3d 859. (See Petitioners' Appendix H, p. 426h.)

The Respondent Board breached its fiduciary duty as trustee to petitioners as well as members of public retirement systems and retirees generally advocating positions on vesting contrary to statutory law and legal precedent. The Board may now have recognized its obligation to protect its members, and has since re versed its adversary attack on members and retirees' rights, and is advocating members have "vested contractual rights" which cannot be abrogated because they are protected by the Contract Clause in the case of *The Legislature of the State of California, et al. v. March Fong Eu,*

Secretary of State, et al, SO19660, pending in the California Supreme Court.

III. Members of defined benefit plans of public retirement systems in California including the LRS acquire a vested contractual right to the specific formula for the calculation of retirement benefits according to the law during their rendition of service whether the State or other governmental entity funds the system on a pay-as-you-go basis or is fully actuarially funded.

The Lower Court erred in holding the Legislators' Retirement System is unique, and in fact the LRS is very similar to the other state systems. Historically the systems have gone from pay-as-you-go to some form of actuarial funding; the current funding mechanisms of the LRS, State Teachers' Retirement System (STRS), and PERS has improved, but none are fully

funded, and the Judges' Retirement System (JRS) is still on a pay-as-you-go basis. A retiree of a California defined benefit public retirement system, including the Legislators' Retirement System, has acquired a contractual right to a specific formula for the calculation of retirement benefits which cannot be altered or amended without comparable offsetting benefits. A state that fails to meet its pension obligations either through repudiation or failure to appropriate funds has both breached its contract to those with vested pension rights and has violated the Contract Clause of the Federal Constitution.

Amicus Curiae respectfully submit that the authority as set forth by the Lower Court which in effect overrules decisions by the California Supreme Court and impairs vested contractual rights

contrary to decisions of this Court is of such importance that it should be viewed in the light of its application not only to Petitioners in the LRS but also to others in the public retirement systems who would be equally affected. The decision places all retirement benefits in jeopardy. PERS has already cited this opinion in pending cases in opposition to pension rights asserted by employees and retirees, e. g., Walsh v. Board of Adm. of PERS, 3 Civil No. C008704.

ARGUMENT

I. THE LEGISLATIVE RETIREMENT SYSTEM IS A CONTRACT BETWEEN THE STATE AND ITS MEMBERS, PROTECTED FROM IMPAIRMENT BY THE CONTRACT CLAUSE OF THE UNITED STATES CONSTITUTION

A. THE CONTRACT CLAUSE PROTECTS RETIREMENT BENEFITS

The Contract Clause of the United States Constitution, Article I, Section 10, provides: "[n]o State shall . . .

pass any . . . Law impairing the Obligation of Contracts . . . ."

Pension rights, unlike other terms of public employment, which are purely statutory, arise from contract and thus are protected from impairment by the Contract Clause. *Kern v. City of Long Beach* (1947) 29 Cal.2d 848, 853; *Carmen v. Alvord* (1982) 31 Cal.3d 318, 325 & n.4 ("Pensions are an obligation of great importance. They help induce faithful public service and provide agreed subsistence to retired public servants who have fulfilled their employment contracts.") The California Supreme Court has held the right to a pension to be a fundamental right. *Strumsky v. San Diego County Employees Retirement Ass'n* (1974) 11 Cal.3d 28, 45.

The Contract Clause protects the

"reasonable pension expectations" of members of the LRS, which are defined by the terms of the contract between the State and LRS members. *Home Building & Loan Association v. Blaisdell*, 200 U.S. 398, at 439 (1934). This contract arose when LRS members first began performing services as Constitutional officers. *Miller v. State of California* (1977) 18 Cal.3d 808, 817 ("Upon acceptance of public employment, [one] acquire[s] a vested right to a pension based on the system then in effect." (Emphasis added).

When these retirees accepted their public employment as State officials and voluntarily joined the LRS, the law provided that their basic allowance would be calculated upon the salary of the current incumbent.

B. A CONTRACTUAL PENSION OBLIGATION IMPLIES ADEQUATE FUNDING AND ADMINISTRATION OF THAT PENSION; AND FAILURE OR REFUSAL TO FUND THAT PENSION UNCONSTITUTIONALLY IMPAIRS THE RETIREMENT CONTRACT

The Lower Court misconstrued the case of *Valdes v. Cory* (1983) 139 Cal.App.3d 773. It represented one of the first California court decisions regarding the rights of retirement system members to some certain employer contributions. In *Valdes*, cutbacks in the state's contribution to the Public Employees' Retirement Fund by the Legislature violated an implied contract between public employees and the state, and therefore violated the Contract Clause. Thus in some circumstances the employees may have a vested right to a particular funding mechanism. However, that is just one of their bundle of vested rights. The funding mechanism is not a required element for a vested

contractual right to a pension held out by a retirement system. It is a separate and distinct right. The funding protects the pension.

Another California Appellate opinions also held that adequate funding of pension liabilities are implied terms of pension contracts, the breach of which will violate the Contract Clause. In *California Teachers Ass'n v. Cory* (1984) 155 Cal.App.3d 494, the Legislature had reduced its annual contribution to the State Teachers' Retirement Fund to $1 as a cost saving measure. The California Supreme Court held that the statutorily-established system contractually obliged the state to provide pension benefits, and that there was an implied contractual duty to adequately fund the system. "Pension rights can encompass the funding mechanism for the pension where

there is a palpable element of exchange involving funding [:] continued service as a teacher in return for enhanced assurance that funds to pay the pension benefits will be available at retirement." (Id. at p. 506.) Consequently the Court issued a writ of mandate compelling the state controller to transfer money into the pension fund according to a previously established statutory formula.

The highest court in at least four other jurisdictions have found that a state's pension obligations imply an obligation to provide for the financial soundness of the fund. *In Gaglione v. Levitt* (N.Y. 1975) 337 N.E.2d 592, the Court of Appeals held that legislatively mandating the State Controller to use state employee retirement funds to purchase "MAC" bonds, issued to bail New

York City out of its financial crisis, violated the "impairment" clause of the state constitution. (The clause provides that state employee pension benefits are contractual obligations not to be impaired.) The court reasoned that by removing discretion from the Controller to place pension funds in whatever investment was prudent, the Legislature was jeopardizing the financial soundness of the fund and therefore impairing the pension contract.

Similar reasoning was used by the Washington Supreme Court when it issued a writ of mandate to require the State Controller to continue adequate funding of the Washington State Treachers' Retirement System, after the Governor had sought to reduce contributions from the general fund. *Weaver v. Evans* (1972) 494 P.2d 693. The Pennsylvania

Supreme Court affirmed in large part a writ of mandate to compel defendant city to make contributions to plaintiff/ employee's pension plan so as to make it actuarially sound, as required by the city charter. *Dombrowski v. Philadelphia* (Penn. 1968) 245 A.2d 238. And the Wisconsin Supreme Court has held that use of state teachers' retirement fund money to fund a study of the retirement fund, where the money used was supposed to have been held in reserve to bolster the soundness of the fund, violated the contractual and statutory rights of the fund members. (Wisc. (1960) 106 N.W.2d 301.)

Taken as a whole, these cases hold that states may not repudiate their pension obligations by underfunding or otherwise tampering with the soundness of the fund. A state pensioner faced

with a bankrupt fund would have a contractual right of action against the state--both to sue for his individual benefits, if he is entitled to these at the time of the action, and to enjoin the Legislature from continuing its neglect of the fund. These holdings are in accord with the California *Valdes* and *Cory* cases, cited above, which strongly affirm the contractual nature of the state's pension obligations and which permit alteration of the fund only when reasonable. See *Allen v. City of Long Beach* (1955) 45 Cal.2d 128. To hold otherwise such as the Lower Court's opinion herein will result in the anomoly that states cannot repudiate their pension obligations outright without violating the Contract Clause, but can repudiate them through the back door by failing to provide a specific funding

mechanism or appropriate money for pension funds. Although overlooked by the Lower Court, it must be emphazied that the Legislature has appropriated the funds for these petitioners.

C. LEGISLATURE INTENDED TO BIND ITSELF CONTRACTUALLY TO FUND THE LRS WHEN THE SYSTEM WAS ESTABLISHED

The statement in the Lower Court's opinion that the Legislature disclaimed any intent to bind itself contractually to fund the LRS is unconscionable. (Appendix A, p. 68a of Petition.) It makes a mockery of every employment contract between the State and its employees requiring performance only on the part of the employee. Gone is the mutuality of contract. Our laws apply equally to both parties of the employment contract. By establishing the System, the Legislature obligated the State to fulfill its part of the

employment contract; binding the State in the future exercise of its taxing and spending powers. *Bellus v. City of Eureka* (1968) 69 Cal.2d 336.

Government Code Sec. 9358 as originally enacted provided that the State shall contribute annually to the Legislators' Retirement Fund, an amount calculated to equal the benefits to be paid during the year. The State as the Employer had the obligation to pay retirement benefits as they fell due just as salaries, but it had the discretion to select its funding mechanism. Originally, it chose the system of pay-as-you-go and appropriated adequate funds annually. The LRS is rather unusual because the Legislature in 1977 funded in total the actuarially determined obligation of the LRS which included all the petitioners' accrued

benefits at June 30, 1976. The calculation of their retirement benefits over their lifetimes for the determination of the required amount to fund the actuarial liability was based upon incumbent salaries as payments fall due.

The Lower Court totally ignored the fact that moneys have been appropriated to pay the petitioners' retirement benefits in accordance with the formulae during their rendition of service.

II. THE LRS IS NOT UNIQUE, AND ANY DEFINED BENEFIT SYSTEM MAY BE ADVERSELY AFFECTED BY THE OPINION OF THE APPELLATE COURT

The LRS is administered by the Respondent Board. The Board is required to administer the LRS as if it were governed by the laws that govern the Public Employees' Retirement System. Gov. Code Sec. 9353 provides as follows:

> This system [the LRS] shall be administered by the Board of Administration of the Public

> Employees' Retirement System. **The board shall administer this system in accordance with the provisions of the Public Employees' Retirement Law to the same extent and with the same effect as if those provisions are contained in the Legislators' Retirement Law...** (Emphasis added.)

The LRS is not unique. It is a defined benefit plan with benefits based upon years of service, age, and compensation. It is administered the same as PERS, to the same extent and with the same effect as though the provisions of the Public Employees' Retirement Law were repeated verbatim in the LRL. The statutory law and decisional law with regard to vesting of benefits and any modifications of benefits are the same.

The lower courts' opinion is an aberration from the decisional law laid down by the California Supreme Court which will deleteriously effect vested contractual benefits. Contrary to the

court's opinion, this decision will impact tens of thousands of retirees as well as active employees in public and private systems. The court in an uninformed manner without all the facts sought to differentiate the LRS among the JRS, the State Teachers' Retirement System (commonly known as STRS, not TRS as referred to by the court); and PERS to a limited extent. The Eleventh Annual Report of Financial Transactions Public Retirement Systems for the Calendar Year 1988/Fiscal Year 1988-89 in California includes data and information based on actuarial information and audited financial statements on 5 statewide systems, 20 systems under the County Employees' Retirement Law of 1937, 2 independent county systems, 34 city systems and 57 special district systems; and there are literally hun-

dreds of other public systems in California. The court's opinion does not analyze these other systems and the destruction of vested rights that this decision will cause if governing boards or voters in times of financial stress seek to modify pension benefits of retirees as well as employees based on this opinion.

A. THE RESPONSES AND BRIEFS FILED BY REPONDENT BOARD IN THESE MATTERS HAVE BEEN A BREACH OF FIDUCIARY DUTY TO MEMBERS OF THE RETIREMENT SYSTEMS ITS REPRESENTS

The positions advocated by the Attorney General as the Attorney for Respondent has been a breach of fiduciary duty, e.g., that retirees' benefits were not vested, or that prior to January 1, 1978, the Legislature had not irrevocably committed California's taxing and spending powers to funding the Legislature's Retirement Fund.

These positions were contrary to the law as it has been applied and represented by PERS to its members in accordance with decisions such as *Betts*. The adversary advocacy in order to "win" the case is contrary to the Board's Fiduciary obligations which have been enunciated in *Hittle v. Santa Barbara County Employees Retirement Assn* (1985) 39 Cal.3d 374.

Congress has been seeking to extend ERISA's fiduciary standards to the public sector, and an adverse decision in this case gives impetus to this movement. The Lower Court's decision herein must be reversed by this Court if public members and retirees are to be protected presently. Now the control of public retirement systems is clearly in the hands of the employer. The result is a bifurcation of responsibility in

the administration of public retirement systems that stand clearly in direct conflict with ERISA which protects employees in private retirement systems. The basic conflict evolves when the public employer fails to recognize the interest of the pension system members and their beneficiaries as being paramount, with the operation and management of the retirement systems accomplished solely in and for their interests.

The arguments advanced in Respondent's Second Supplemental Brief answering the Lower Court's questions is contrary to the interest of pension system members and their beneficiaries of California public retirement systems and a direct conflict of interest. Under the theory advanced, the retirees of all systems who served during the period of pay-as-you-go financing could

have their pension benefits substantially reduced by the Legislature's failure to fund them. Since none of the State systems are fully actuarially funded, would any pension benefit be secure? No, all would be in jeopardy!

It is noteworthy that after the Board's attention has been drawn to the fiduciary duty they owe as trustees to members and retirees, Respondent has taken the opposite position in the pending case of The Legislature of the State of California, et al. v. March Fong Eu, Secretary of State, in the California Supreme Court, No. SO19660. Their brief recognizes that prior to the passage of Proposition 140, on November 6, 1990, affecting members' LRS pension benefits, effective on November 7, 1990, LRS members had vested rights to earn benefits under the terms set

forth in the LRS. For example, on page 11 of the Return of Respondent Board of PERS to Alternative Writ of Mandate dated April 16, 1991, is the following:

> C. LRS Members as of November 6, 1990 had a Vested Right to Earn Benefits under the Terms set Forth in the LRS
>
> 1. Pension Benefits Vest Before They Are Earned
>
> **III. RETIREES' ACQUIRED CONTRACTUAL RIGHTS TO A SPECIFIC FORMULA FOR THE CALCULATION OF THEIR BASIC RETIREMENT BENEFITS BASED UPON THE FLUCTUATING FORMULA TIED TO INCUMBENT SALARIES WHICH CANNOT BE IMPAIRED**

The California law is set forth in the California Supreme Court's decision of *Olson v. Cory* (1980) 27 Cal.3d 532; 540-541:

> "A long line of this court's decisions has reiterated the principle that a public employee's pension rights are an integral element of compensation and a vested contractual right accruing upon acceptance of employment. (*Betts v. Board of Administration, supra,* 21 Cal.3d 939; *Kern v. City of*

> *Long Beach, supra*, 29 Cal.2d 848, 852-853.) In *Betts*, this court held that a former state treasurer who had served in that office from 1959 to 1967 was entitled to a pension on the basis of the law in effect at the time of his termination rather than the modified law in effect at the time of his application for pension benefits in 1976. . ."
>
> "'An employee's contractual pension expectations are measured by benefits which are in effect not only when employment commences, but which are thereafter conferred during the employee's subsequent tenure.' (*Betts v. Board of Administration, supra*, 21 Cal. 3d 859, 866.)'

The Supreme Court concluded in *Betts,Id,* at p. 867-868 that an amendment enacted after he had left office which purported to convert a fluctuating basic pension allowance to a fixed allowance "could not constitutionally be applied to petitioner because the amendment withdrew benefits to which he earned a vested contract while employed. No 'comparable

new advantages' to petitioner appear in the plan which can offset the detriment he has suffered by replacement of a 'fluctuating' system of benefit computation with a 'fixed' system." The Lower Court herein should have reached the identical results.

Members of public retirement systems are to have their retirement allowances calculated according to the formula in place during their rendition of service and this formula cannot be altered or amended to their detriment after their retirement without violating the Contract Clause of the federal Constitution irrespective of the funding mechanism selected by the employer.

A. THE DIMUNITION OF A RETIREMENT ALLOWANCE BY AMENDING A RETIREES' FORMULA FOR THE CALCULATION OF RETIREMENT BENEFITS IS CONTRARY TO THE PUBLIC POLICY AND PURPOSE OF CALIFORNIA'S RETIREMENT LAWS

One of the primary objectives in providing pensions for public employees is to induce competent persons to enter and remain in public employment. *Bilyeu v. State Employees' Retirement System* (1962) 58 Cal.2d 618 at p. 623. In *Knight v. Board of Administration of the State Employees' Retirement System* (1948) 32 Cal.2d 400, 405, the Court said:

> "One of the purposes of a retirement system is an inducement which will enable the government to secure and retain more qualified government personnel. That purpose is more important in the case of officers than ordinary employees when we consider the more important functions they perform."

In one of California's leading cases the Court said in *Kern v. City of Long Beach* (1947) 29 Cal.2d 848, 855, 856:

> ". . .[T]he mere fact that performance is in whole or in part dependent upon certain

> contingencies does not prevent a contract from arising, and the employing governmental body may not deny or impair the contingent liability any more than it can refuse to make the salary payments which are immediately due. Clearly, it cannot do so after all the contingencies have happened, and in our opinion it connot do so at any time after a contractual duty to make salary payments has arisen, since a part of the compensation which the employee has at that time earned consists of his pension rights.
>
> "[To] hold otherwise would defeat one of the primary objectives in providing pensions for government employees, which is to induce competent persons to enter and remain in public employments." [Citations omitted]. . "It is obvious that this purpose would be thwarted if a public employee could be deprived of pension benefits, and the promise of a pension annuity would either become ineffective as an inducement to public employees or it would become merely a snare and a delusion to the unwary." [Citations omitted.]

Elective officers who are members of a retirement plan have the same

constitutional protection against impairment of retirement benefits as do lesser employees. Such benefits as are earned by an elective officer cannot be taken away from him.

What a cruel hoax it would be if the State or any public employer could deny full pension rights earned and vested by failing to fund them or failing to provide a particular funding mechanism. Obviously, such a result shatters public policy and retirement provisions will be ineffective to induce qualified people into public service, and remain there, or they will have become a snare for the unwary as described in *KERN*.

CONCLUSION

This Court has long recognized the special nature and importance of pension rights, particularly in cases where

State law has held them vested, contractual rights. Your Court has subjected attempts to impair them to careful scrutiny under the Contract Clause. Application of that careful scrutiny and review of the Lower Court's opinion herein freed of political ramifications will disclose a violation of the Contract Clause of the federal Constitutuion. Proposition 57 directly and severely impairs the vested pension rights of Constitutional officers who were first elected prior to March 4, 1972, or their surviving beneficiaries. As long as the opinion herein is not reversed, all retirement benefits of public employees and retirees are in jeopardy. Accordingly, Amicus Curiae respectfully requests the Court to protect vested rights threatened by the Opinion rendered by the Lower Court as

it has protected such rights in the past. For the reasons stated, grant the petition for a writ of certiorari to the Court of Appeal of the State of California in and for the Third Appellate District. The judgment must be reversed.

DATED: June 3, 1991.

Respectfully submitted,

ROBERT F. CARLSON AND
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By Robert F. Carlson

ROBERT F. CARLSON

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